Malaysia Monitor

Not Now, Not Now

Malaysia demurs from policy easing

Nov 23, 2016

- **As widely expected, Bank Negara opted to keep its Overnight Policy Rate unchanged at 3.0% today. The recent global currency volatility would likely have played into the consideration.**
- **Like most of us, the central bank appears to be grasping for a sense of President Trump would shape the global growth outlook and the implications for Malaysia's own economy, and therefore its policy rate path.**
- **Given that much is still not known until the man takes office – if even then! – it remains unlikely that BNM would be comfortable easing its OPR in the next meeting ending Jan 19th next year, coincidentally just one day before Trump's inauguration.**

Gotta Figure Him Out

If you stop and think about it, it's only been just two weeks since the world was shaken by Donald Trump's victory. Since then, market has obviously been busy adjusting to a potential sea change in the global market dynamics that his presidency would bring about. A lot of ink has been spilled as market players try to decipher the impact of his policy platform. For the purpose of today's discussion, let's zoom in on the repercussions for Malaysia's economy – and therefore, its potential policy rate path.

Judging from today's BNM policy statement, it appears to us that the central bank too is trying to do just that. In what can be seen as an allusion to Trump's reflationary policy talks, BNM notes that "The prospect of a shift towards progressive use of fiscal policy in the developed economies could lead to a more balanced policy environment that would support growth going forward." Given the relative export dependence of Malaysia's economy, that aspect of Trumponomics is obviously a good thing.

Still, this sunny-side up egg happens to have a burnt flipside. Specifically, the less savoury aspects of Trump's platform present significant risks to Malaysia, with the BNM policy statement adding that "there is uncertainty arising from risks of protectionism and financial market volatility." It remains anybody's guess but if the already-tepid global trade flows become further crimped next year due to tariffs or even threats of them, Malaysia would rank as one of the more highly impacted.

While Trump is a lot more likely to his salvos to the likes of China and Mexico than to Malaysia, it is wishful thinking to assume that the latter would escape unscathed from any protracted and broadened trade wars.

Even if the importance of US as a trading partner to Malaysia has seen a structural decline over the past decade or so, a good 1 out of 10 dollars that Malaysia gets from exports is still coming directly out from American demand. Moreover, any impact on China's growth arising from its own bilateral trade skirmishes with the US, would have an indirect – but unfortunately not insignificant – impact on Malaysia's exports, as well.

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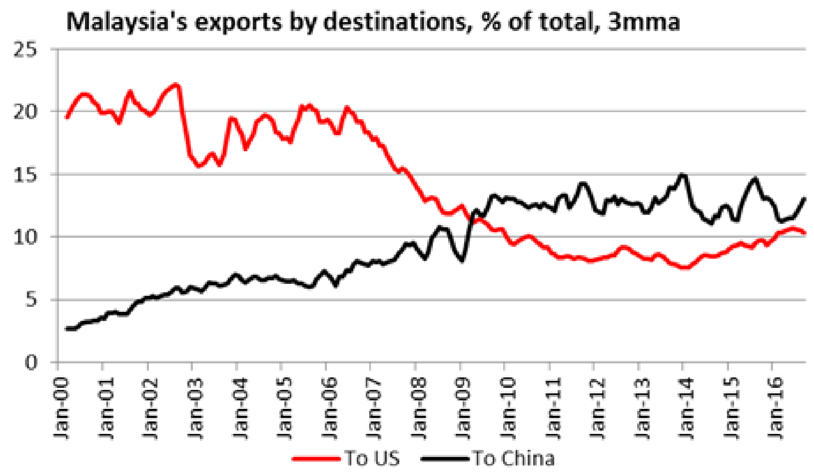
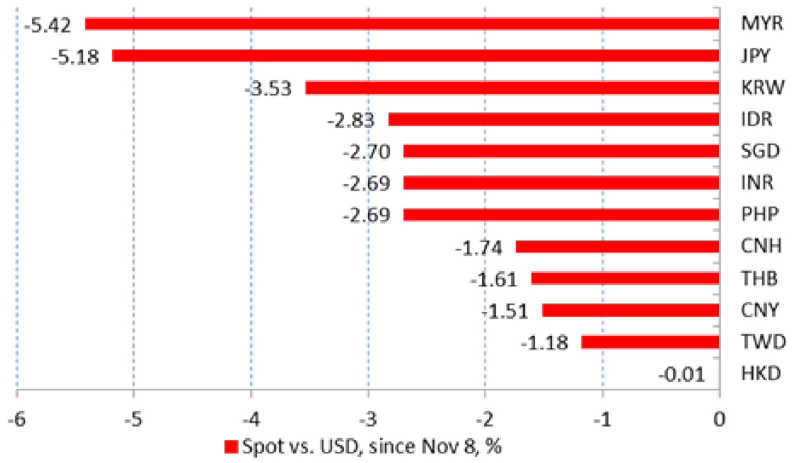


Source: Bloomberg, OCBC. Note: 3mma denotes 3-month moving average figures.

With external risks on the rise, it would have been ideal if the BNM has the opportunity cut its policy rate further to give more oomph to domestic demand as a counterbalance. This is especially so, given that from a purely domestic angle, there is space given by the relatively low inflation. CPI headline inflation printed just 1.5%yoy in September and is projected by BNM to "remain relatively stable in 2017 given the environment of low global energy and commodity prices and generally subdued global inflation."

Still, even if talking about the demise of globalization seems to be a new cottage industry now, we still very much live in an inter-connected world at this point, where policymakers have to keep global, not just domestic, factors in mind. In the case of the monetary policy decision today, for instance, BNM would likely have noted the impact of resurgent US yields on the financial markets in general and EM currency volatility in particular. Indeed, at this stage, ringgit carries the unfortunate moniker of being one of the worst performing Asian currencies since the US election – a phenomenon that today's statement ascribes to being driven by "continuing uncertainties in global economic and policy environment, and geopolitical developments."



Source: Bloomberg, OCBC.

Long story short, in such an unsettled global environment, even if Bank Negara feels that it has the space given by domestic factors to ease further, it is probably wise refrain from doing so for now. That holding pattern, lamentably, might have to take place for a while more. The next BNM meeting would end on January 19th, 2017. Given that this would be just one day before Trump is due to be sworn in, it is rather unlikely that we would have a clear sense of just how he would act when does actually become the president – and all the market repercussions that come with it. Hence, there is a very little chance to see BNM opening 2017 with a rate cut, but probably the market would have adjusted well to the eventuality by the time BNM meets again in early March for it to proceed with easing once more. Call that our 2017's New Year Wish, perhaps?

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